



VC Deal Structure: The Investment, Mechanics and Key Terms of a Series A Investment Agreement

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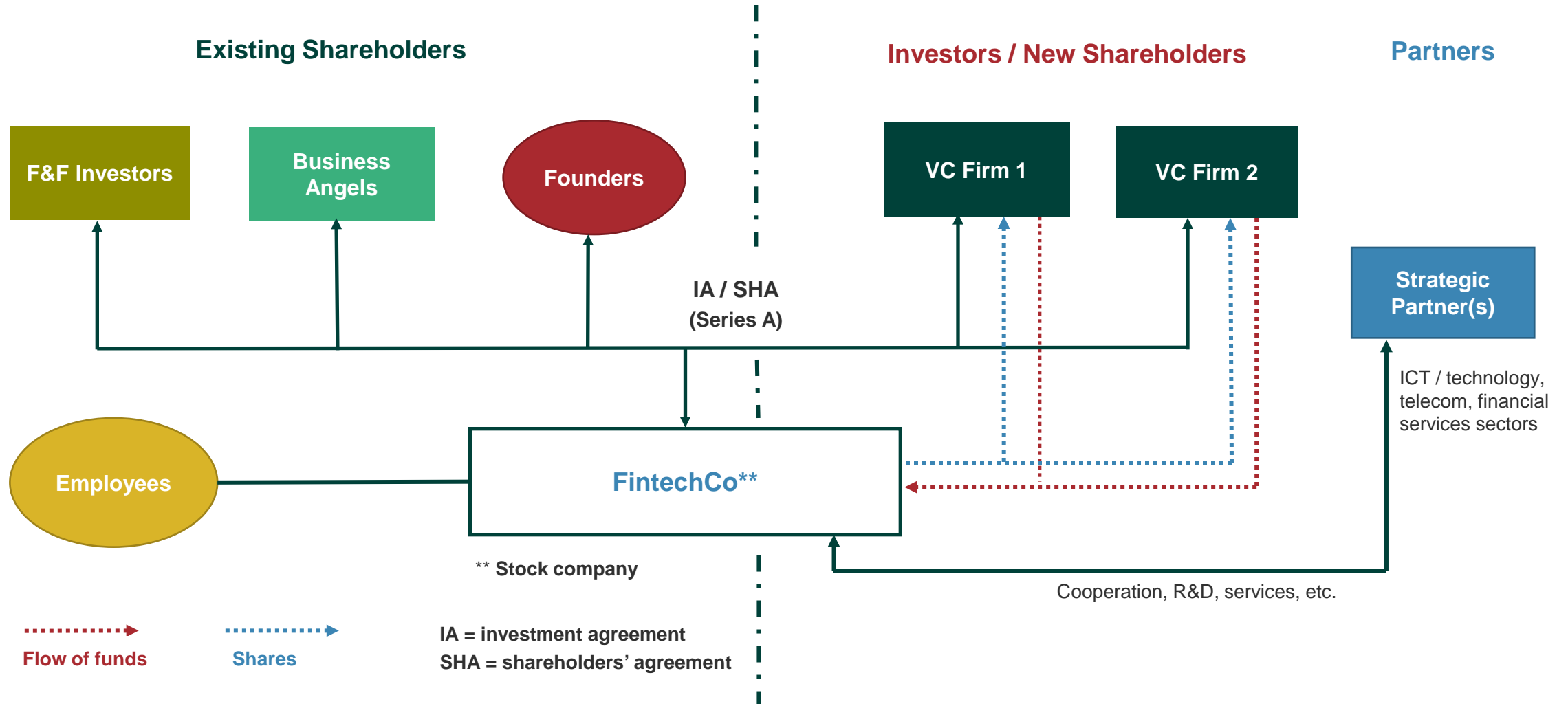


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Case Study – The Series A Financing Round at a Glance

Simplified overview



Structure and Mechanics of Series A Investment

FintechCo

- Startup in financial services industry
- Stock company (e.g. Swiss stock corporation)
- Pre-financing: single category of (common) registered shares

The investment by VC Firms

- Direct equity investment into FintechCo
- Series A preferred shares

Structure of Series A financing round

- Capital increase (issuance of new shares)
- Investment and subscription agreement (IA)
- Shareholders agreement (SHA)
- Corporate documents:
 - Articles of incorporation
 - Organization by-laws

Legal basis for investor rights and preferences

- Corporate / securities laws (incl. articles, organization by-laws) **and**
- Contracts (IA, SHA)

Snapshot on Contractual Framework: IA vs. SHA

IA – key aspects

a) Terms of investment, equity structure

b) Obligations of parties:

- Existing shareholders: implementation of capital increase, waiver of preferential subscription rights
- Investors: subscription and payment of committed amounts for new shares
- Company: ancillary undertakings (e.g. covenants)

c) Conduct of business until closing

d) Closing, incl. conditions precedent

e) Termination and rescission

f) Representations and warranties

g) Remedies

h) Confidentiality; nature of parties rights and obligations, etc.

i) Governing law, dispute resolution



SHA – key aspects

a) Governance matters:

- Articles, organization by-laws
- Control, minority protection, important matters
- Composition board of directors / management
- Information rights

b) Business related matters

c) Further financing

d) Capital structure, rights of shareholders
(e.g. preferences, anti-dilution protection)

e) Exit provisions, share transfers

f) Enforcement (e.g. liquidated damages)

g) Term, termination

h) Non-competition

i) Governing law, dispute resolution

IA – The Parties, Subject Matter and Applicable Law

Parties to the IA

(1) Investors

- (foreign) VC Firms (e.g. in the form of LLPs or other investment vehicles)

(2) Existing shareholders

- Founders
- F&F investors
- Business angels

(3) The company (FintechCo)

Subject matter of IA

- Financing agreement
- Main obligations
 - **Investors**: Subscription and payment of committed amounts for new series A pref. shares
 - **Existing shareholders**: Waiver of preferential subscription rights, procure resolutions of shareholders and board of directors, implementation of capital increase
- Ancillary obligations
 - **Existing shareholders**: Representations and warranties, covenants, etc.
 - **FintechCo**: Confidentiality, conduct of business

Cross-border setting; applicable law

- Interplay between IA / SHA and (mandatory) corporate law framework

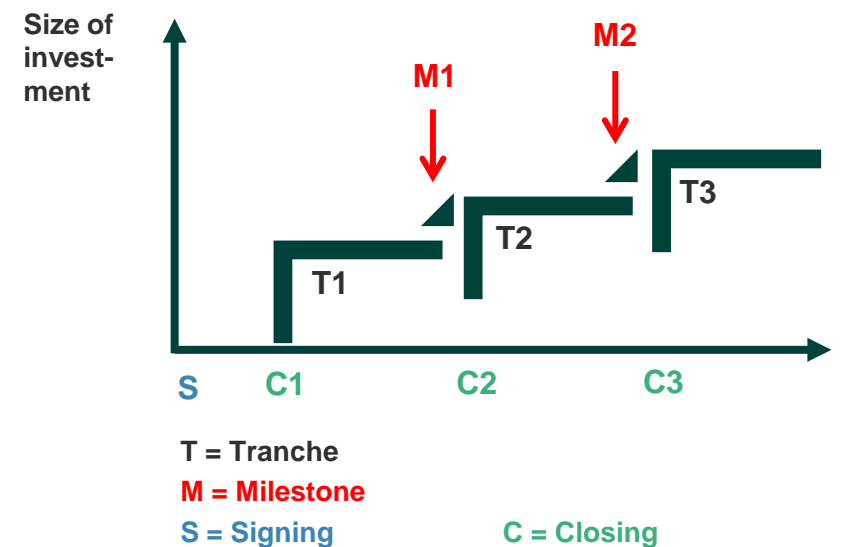
Funding approach and commitment by VC Firms

- (1) Funding in one tranche (one closing) OR
- (2) Funding in several tranches (multiple closings, milestone approach)

Milestone funding approach

- **Purpose**
 - Investment control
 - Incentivise the management
- **Mechanics**
 - Staggered investment
 - Funding in tranches subject to achievement of milestones
- **Milestones**
 - Objective measurable criteria
 - Decision on achievement
 - Investors
 - Board of directors of FintechCo
 - Independent expert
- **Staggered legal implementation**
 - Multiple capital increases OR
 - Staggered payment of issue price for shares (partial «paying-up») OR
 - Subsequent contributions to reserves

Staggered investment / funding



Conditions to closing

- Availability of all required documents for closing
 - Capital increase
 - Corporate changes (e.g. board change, appointment of auditors)
- No breach of IA
- No material adverse change (MAC)
- Specific requirements (e.g. consents from third parties, fulfillment of milestones for tranches)
- Bring-down certificates (e.g. reps/warranties)

Closing and post-closing

- Place and date of closing
- Closing of IA: closing actions and deliverables (incl. SHA)
- Local law formalities / capital increase (e.g. involvement of notary public, deposit of funds)
- Registration of capital increase (e.g. public commercial register)
- Issuance of shares and updating of share register of FintechCo

Termination and rescission

Purpose

- Allocation of risks
- Bridge information asymmetry
- Obtain additional information, disclosures
- Differences: VC transaction vs. M&A deal

Representations by existing shareholders

- Expectations of investors >> standard set of reps/warranties
- Who is best positioned? >> Founders vs. F&F investors vs. BA?
- Appropriate solutions?

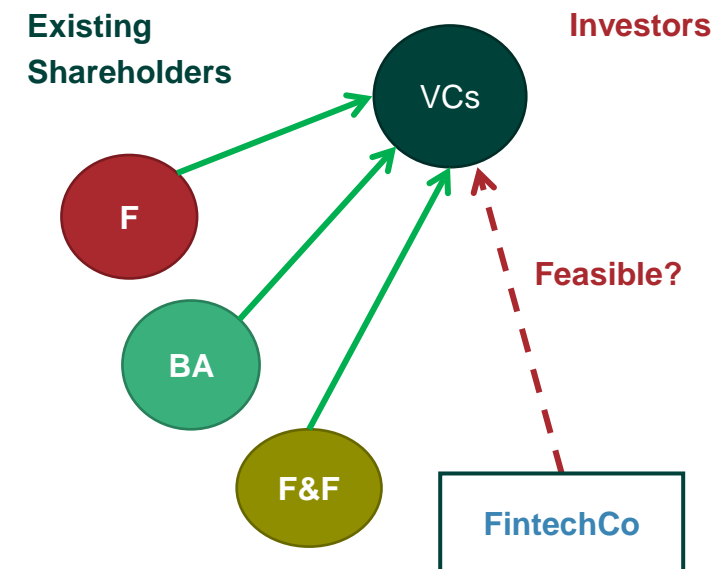
Representations by Swiss company (FintechCo)?

- Nature of equity investment
- Corporate law restrictions
 - Prohibition of return of capital
 - Unlawful distribution of profits

Representations by investors

Exclusive representations and warranties

Reps / warranties for investors



VCs = VC Firms

F = Founders (and managers)

BA = Business angels

F&F = Family & friends

Remedies

- Right to remedy / cure
 - >> To put company and/or investor(s) in a position as if no misrepresentation or breach had occurred
- Indemnification / payment of damages
- Transfer of shares from existing shareholders to investors
- Staggered remedy concept

Limitations

- Time limitations (notice of breach, limitations on claims)
- Limitations on liability
 - Liability cap
 - Disclosed matters (e.g. fair disclosure concept)
 - Other limitations (insurance coverage, provisions, etc.)

Remedies exclusive

Practical challenges

«Boiler plate» items

- Nature of parties' rights and obligations
 - Several, not joint, except as otherwise set forth in IA
 - Investors may exercise and enforce their rights individually
 - Obligations of contractual nature, no simple partnership
- Costs, expenses, taxes
- Choice of law, dispute resolution

VC documentation

- Expectations of parties
- Alignment on VC standards / typical deal terms
- Use of model documentation for VC investments (as starting point)
- Allocation of drafting responsibility (!)

Recent developments and trends



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